

EXTERNAL AUDIT CIRCULAR No. 10



CONNECTICUT DEPARTMENT OF TRANSPORTATION

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SUBJECT: Interest and Other Financial Costs and Facilities Capital Cost of Money

Release Date: June 1, 2011

This Circular presents interpretative guidance regarding interest, other financial costs, and facilities capital cost of money and includes examples for use in determining the allowability of such costs. Please refer to Chapter 8.6, 8.7, 8.12, 8.16, 8.23, 8.28 and 11.4H of the 2010 edition of the AASHTO Uniform Audit & Accounting Guide for additional guidance.

ISSUES

During an incurred-cost/pre-award audit, the auditor may encounter interest costs that are included in a consultant's indirect costs. Additionally, as part of the indirect cost rate-submission process, a consultant may propose a charge rate for Facilities Capital Cost of Money (FCCM).

ALLOWABILITY

A. Interest and Other Financial Costs

The following types of costs are expressly unallowable: interest costs associated with the borrowing of money (however represented), costs of financing or refinancing of capital (including interest associated with capital leases), legal and professional fees paid in connection with preparing prospectuses, and costs of preparing and issuing stock rights.

B. Facilities Capital Cost of Money (FCCM)

Although interest costs associated with the financing of capital are unallowable, FCCM [an imputed cost] is allowable. FCCM is not required to be recorded in the consultant's formal accounting records; instead, FCCM is computed as a charge rate based on the following factors:

- The average annual net book value of the consultant's investments in the fixed assets used for allowable business activities as established by the Cost Principles of FAR Part 31,
- The prorated average Prompt Payment Act Interest Rate determined by the Secretary of the Treasury for the accounting period in question, and
- The consultant's direct labor base used to determine indirect cost rates.

FCCM may be considered to be an indirect expense associated with the general indirect cost pool; however, FCCM should be a separately identified charge rate and should *not* be included as part of the submitted indirect cost rate.

COMPLIANCE REQUIREMENTS

Consultants **who propose** an FCCM rate must submit a completed schedule with detailed computations supporting the rate. An acceptable format for the FCCM schedule is provided in the Indirect Cost Rate Excel Schedule [Cost of Money tab]. All submitted information is subject to verification by CTDOT auditors.

EXAMPLES

Example 10-1. *Consultant W* financed a new machine under a capital lease agreement. The lease terms provide for *Consultant W* to make annual year-end payments of \$35,000 for all 8 years of the machine's useful life. Each payment includes 9 percent interest. At the end of 8 years, the firm has the option to purchase the machine for \$100.

Analysis: Although the yearly depreciation associated with leased equipment may be included in the indirect cost pool, the entire \$35,000 yearly payment must be excluded from the indirect cost pool. (Note: Interest is unallowable, and the amortization of the capital lease results in a reduction to a liability account—not an expense.)

Example 10-2. For the year ended December 31, 2009, *Consultant Z* incurred \$700,000 of direct labor costs. At beginning of the 2009, the net book value (NBV) of the fixed assets (property, plant, and equipment) used by the firm was \$135,000. By the end of 2009, the NBV of the fixed assets increased to \$175,000.

Analysis: Use the Indirect Cost Rate Excel Schedule [Cost of Money tab], to determine the amount *Consultant Z* is entitled to include as FCCM in the Indirect Cost Rate Schedule and may charge for each dollar of direct labor incurred in the performance of CTDOT contracts [unless specifically excluded].

Example 10-3. An audit of *Consultant Z's* year-2009 overhead costs revealed that 20 percent of the miles driven in automobiles owned by firm related to personal commuting and/or unallowable marketing activities. Accordingly, the firm must adjust its FCCM rate. As a result of the adjustment, the net book values for the fixed assets at the beginning and end of 2009 were \$118,000 and \$165,500, respectively.

Analysis: Only the portion of fixed assets used for allowable business activities within the meaning of FAR Part 31 may be included in the FCCM computation. Accordingly, *Consultant Z* must disallow 20 percent of the automobiles' carrying value. Use the Indirect Cost Rate Excel Schedule [Cost of Money tab], to determine the amount *Consultant Z* is entitled to include as FCCM in the Indirect Cost Rate Schedule and may charge for each dollar of direct labor incurred in the performance of CTDOT contracts [unless specifically excluded].

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REFERENCES

- FAR 31.205-10 (general Cost of Money clause), see also 48 CFR 9904.414 (also known as CAS 414; includes criteria for measurement, assignment, and allocation of Cost of Money; FAR 31.205-10 makes CAS 414 applicable to all contracts, even contracts which are not CAS-covered or are subject to modified CAS coverage).
- FAR 31.205-20 (Interest and Other Financial Costs).
- Prompt Payment Act (Public Law 97-177) (sets interest rate to be used for Cost of Money Computations).
- DCAA Contract Audit Manual § 8-414 (Cost of Money as an Element of the Cost of Facilities Capital).
- CTDOT External Audit Circular No. 1 (definitions, audit authority, and general guidance regarding the computation of indirect cost rates).
- Link to Prompt Payment Interest Rate <http://www.fms.treas.gov/prompt/rates.html>
- AASHTO Uniform Audit & Accounting Guide [2010 Edition]